



COUNTY OF LOS ANGELES  
OFFICE OF THE COUNTY COUNSEL

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TO: SUPERVISOR ZEV YAROSLAVSKY, Chairman  
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SUPERVISOR YVONNE BRATHWAITE BURKE  
SUPERVISOR DON KNABE  
SUPERVISOR MICHAEL D. ANTONOVICH

FROM: LLOYD W. PELLMAN  
County Counsel

RE: **Entertainment Industry Development Corporation--  
Letter from District Attorney and Retention of Attorneys  
for the Corporation and its Directors and Officers**

This second report concerning the Entertainment Industry Development Corporation of Southern California ("EIDC") focuses on the EIDC's retention of counsel and payment of legal fees for the corporation and its directors and officers. This report was prepared in response to a request from Supervisor Yaroslavsky's office for our advice concerning a letter from District Attorney Steve Cooley, dated September 16, 2002.

In the letter, the District Attorney asserts that the EIDC is a public entity and, as a public entity, section 995.8 of the California Government Tort Claims Act ("Tort Claims Act") requires certain findings be made prior to the EIDC providing funds to pay for the criminal defense of any employee of the entity.

As discussed in the attached report, we believe that the Tort Claims Act does not apply to the EIDC. The EIDC is a non profit public benefit corporation, which is an entity that is not included in the definition of "public entity" under the Tort Claims Act.

Although it is our opinion that the provisions of the Tort Claims Act do not apply to the EIDC, there are other specific provisions in the California Corporations Code that identify the parameters by which the EIDC may pay for the legal fees incurred by its officers or directors. In addition, EIDC's bylaws have specific provisions that address this same issue. Although not identical, these provisions are similar to the Tort Claims Act with respect to when and how the EIDC may pay for the legal fees incurred by its officers or directors.

Although we are pleased to provide you with the enclosed report, please note that our office does not represent the EIDC or its board of directors, officers or employees. Therefore, legal advice pertaining to your obligations as an EIDC director should properly be directed to the EIDC's general counsel, Ms. Donna Wells.

If you have any questions concerning these issues please contact me, Donovan Main at 974-1829, Roberta Fesler at 974-1861, or John Krattli at 974-1838.

LWP:JFK:dm

Enclosure

c: David E. Janssen  
Chief Administrative Officer

Violet Varona-Lukens, Executive Officer  
Board of Supervisors

SECOND REPORT TO THE BOARD OF SUPERVISORS  
CONCERNING THE ENTERTAINMENT INDUSTRY  
DEVELOPMENT CORPORATION OF SOUTHERN CALIFORNIA  
(District Attorney's Letter, Retention of Attorneys and Payment  
of Legal Fees for the Corporation and its Directors and Officers)

This second report concerning the Entertainment Industry Development Corporation of Southern California ("EIDC") focuses on the EIDC's retention of counsel and payment of legal fees for the corporation and its directors and officers. This report was prepared in response to a request from Supervisor Yaroslavsky's office for our advice concerning a letter from District Attorney Steve Cooley, dated September 16, 2002. In the letter, the District Attorney asserts that the EIDC is a public entity and, as a public entity, section 995.8 of the California Government Tort Claims Act ("Tort Claims Act") requires certain findings be made prior to the EIDC providing funds to pay for the criminal defense of any employee of the entity.

We have considered the District Attorney's position and believe that the Tort Claims Act does not apply to the EIDC. Although it is our opinion that the provisions of the Tort Claims Act do not apply to the EIDC, this issue might be somewhat moot, as the California Corporations Code, which we believe is applicable, contains language similar, although not identical, to the Tort Claims Act.

The Office of the County Counsel does not represent the EIDC or its board of directors, officers, or employees. The EIDC is represented by its general counsel, Ms. Donna Wells. In addition, we understand that the EIDC has retained the services of two criminal defense attorneys, Mr. George Newhouse of Thelen Reid & Priest, LLP, and Mr. Tom Brown of Sheppard, Mullin, Richter & Hampton, LLP. Mr. Newhouse informed us that he and Mr. Brown were retained to represent the interests of the EIDC as a corporation and not retained to represent the interests of any individual. We understand, therefore, that Mr. Cluff does not at this time have a separate attorney representing him.

I. The Tort Claims Act

In Mr. Cooley's letter, he asserts that section 995.8 of the Government Code applies to the EIDC and should be considered by the EIDC board in determining whether to provide a legal defense to an EIDC director or officer. Section 995.8 provides, in pertinent part, the following:

"A public entity is not required to provide for the defense of a criminal action or proceeding . . . brought against an employee or former employee, but a public entity may provide for [such a defense] if: (a) the defense of a criminal action or proceeding is brought on account of an act or omission in the scope of his employment as an employee of the public entity; and (b) the public entity determines that such defense would be in the best interests of the public entity and that the employee or former employee acted, or failed to act, in good faith, without actual malice and in the apparent interests of the public entity."

Section 995.8 only applies to a "public entity" as defined under the Tort Claims Act. Section 811.2 of the Tort Claims Act defines a public entity to include the following: the State of California, the Regents of the University of California, a county, a city, a district, a public authority, a public agency, and any other subdivision or public corporation in the State.

As confirmed in its articles of incorporation filed with the California Secretary of State, EIDC is organized under the California Corporations Code as a nonprofit public benefit corporation. A nonprofit public benefit corporation is not expressly included in the definition of public entity under the Tort Claims Act, and therefore, section 995.8 does not apply to the EIDC.

Unlike a nonprofit public benefit corporation, the entities identified as "public entities" under the Tort Claims Act enjoy sovereign immunities that would shield them from lawsuits except for the existence of the Tort Claims Act. The Tort Claims Act represents a limited waiver of sovereign immunity to bring tort claims against the State of California and its public entities, including municipalities. A party who wants to bring an action against a governmental entity must comply with the detailed procedural requirements enumerated in the Tort Claims Act, such as presenting a timely claim to the public entity. EIDC does not possess sovereign immunity and, therefore, there is no need for the Tort Claims Act to apply to it.

## II. The California Corporations Code and the EIDC Bylaws

Although we do not believe that the Tort Claims Act applies to the EIDC, the California Corporations Code contains similar provisions for when and how a nonprofit public benefit corporation may pay the legal fees incurred by one of its officers or directors.

Section 5238 of the Corporations Code prescribes when a nonprofit public benefit corporation can pay the legal fees incurred by one of its directors, officers or employees, referred to in the code as "agents." If the agent is successful on the merits in defense of the proceeding, section 5238(d) provides that the corporation shall indemnify the agent against actual and reasonable expenses. If the agent has not successfully defended against the proceeding, section 5238(e) provides that the corporation may indemnify the agent only if the "standard of conduct" is met. One method to determine whether the "standard of conduct" is met is by a majority vote of a quorum of the directors who are not a party to the proceeding. Section 5238(b) specifies the "standard of conduct" as follows: the agent acted in good faith and in a manner reasonably believed to be in the corporation's best interests and, in the case of a criminal proceeding, had no reasonable cause to believe that the conduct was unlawful.

Section 5238(f) of the code provides that a corporation may advance the expenses of an agent incurred in defending an action ". . . upon the receipt of an undertaking by or on behalf of the agent to repay such amount unless it shall be determined ultimately that the agent is entitled to be indemnified . . . ."

Section 5238(h) provides that the corporation shall not indemnify or make an advance to an agent where it appears that "it would be inconsistent with a provision of the articles, bylaws, a

resolution of the members or an agreement in effect at the time of the accrual of the alleged cause of action asserted in the proceeding in which the expenses were incurred or other amounts paid, which prohibits or otherwise limits indemnification." This provision limits the ability of a corporation to indemnify its agent or to advance expenses for its agent if the bylaws expressly prohibit such.

Article 5.12 of the EIDC's bylaws follows the provisions of section 5238 of the Corporations Code, albeit with much less detail. The bylaws are silent, however, as to whether the EIDC can advance legal fees to its directors and officers. Because the bylaws do not specifically prohibit the advancing of legal expenses, it is unclear whether the EIDC can advance such expenses upon receipt of an undertaking as required by the code.

### III. Issues to Consider

EIDC's criminal defense attorney George Newhouse informed us that he and Mr. Brown will notify the EIDC and Mr. Cluff if and when they believe it prudent for Mr. Cluff to obtain his own and separate counsel. However, the EIDC board has the independent authority to make a determination regarding whether EIDC should continue to be represented by Mr. Newhouse and/or Mr. Brown and whether Mr. Cluff and the EIDC should continue to be represented by the same counsel. In making these "business judgments," a director must consider what is in the best interests of the corporation.

We are informed that the EIDC is reviewing its insurance policies to determine whether it has directors and officers insurance. EIDC criminal defense counsel George Newhouse told us he believes that the EIDC might have such insurance but that it might not provide coverage for criminal investigations. He promised to determine whether the EIDC has such a policy and, if so, whether coverage would be afforded for the on going investigation.